REPORT BY THE
AUDITOR GENERAL
OF CALIFORNIA

THE CALIFORNIA HOUSING FINANCE AGENCY HAS GENERALLY COMPLIED WITH STATUTORY REQUIREMENTS IN FINANCING SINGLE-FAMILY HOMES AND MULTIFAMILY RENTAL PROJECTS

P-950

JULY 1991

The California Housing Finance Agency Has Generally Complied With Statutory Requirements in Financing Single-Family Homes and Multifamily Rental Projects

P-950, July 1991

Office of the Auditor General
California

Kurt R. Sjoberg, Auditor General (acting)

State of California
Office of the Auditor General
660 J Street, Suite 300, Sacramento, CA 95814
Telephone : (916) 445-0255

July 31, 1991 P-950

Honorable Robert J. Campbell, Chairman
Members, Joint Legislative Audit Committee
State Capitol, Room 2163
Sacramento, California 95814

Dear Mr. Chairman and Members:

The Office of the Auditor General presents its report concerning the financing of single-family homes and multifamily rental projects by the California Housing Finance Agency.

Respectfully submitted,

Kurt R. Sjoberg

KURT R. SJOBERG
Auditor General (acting)

Table of Contents

Appendices

Illustrations

Summary

Results in Brief

The California Housing Finance Agency (agency) was created to meet the housing needs of persons and families of low or moderate income. To do this, the agency provides low interest loans for the purchase of single-family homes and for the permanent financing of multifamily rental projects. To receive a single-family home loan, borrowers must not have owned their principal residence during the preceding three years, their income must not exceed certain limits, the price of the home must be within certain limits, and the borrowers must occupy the home as their principal residence. To receive a loan for the permanent financing of a multifamily rental project, the developer must set aside a portion of the project's units for households whose income is within various established limits. During our audit we noted the following conditions:

- From July 1, 1985, to June 30, 1990, the agency financed approximately 21,600 loans for single-family homes at an average sales price of approximately $84,300. Approximately 91 percent of these loans were for households of moderate income (usually from 120 to 150 percent of the area median income) and less than 9 percent were for households of very low and lower income (less than 50 percent and less than 80 percent of the area median income respectively). Virtually all of the loans were made to households with the appropriate income levels.

- From July 1, 1985, to June 30, 1990, the agency made loans for the construction of 47 multifamily rental projects with approximately 3,390 housing units. Approximately 1,230 (36 percent) of the units in these projects were restricted to lower or very low income households, a number that exceeded applicable state and federal law. However, seven projects have not submitted reports on the income levels of the occupants of these units. Nineteen other projects have submitted reports that did not list a sufficient number of qualified tenants as required by the projects' regulatory agreements with the agency.

- As required by law, between July 1, 1987, and June 30, 1990, the agency has financed the development of new housing in certain types of demographic areas of the State in the same general proportion as the breakdown of the needs for new housing and rental units for very low or lower income households in these areas as identified in the California Statewide Housing Plan (statewide plan). The agency has not balanced its activities as successfully in awarding loans for the rehabilitation of existing housing units or for the development of all types of rental units for the elderly. The statewide plan is a compilation of goals and objectives for the development of housing in California.

Background

The agency finances most of its programs by selling tax-exempt bonds. As of June 30, 1990, the agency had the authority to have a total value of $4.65 billion in outstanding bonds or notes.

The agency's single-family loan program provides mortgage capital to enable borrowers who meet income eligibility requirements to obtain loans at below-market interest rates. The agency purchases mortgages that lending institutions make to borrowers who are eligible for the agency's programs. Eligible

borrowers apply to lenders or developers for their loans. From July 1, 1985, to June 30, 1990, the agency purchased single-family mortgages with an original loan amount of approximately $1.7 billion.

The agency's multifamily rental program requires developers to provide rental housing for households who meet specific income eligibility requirements. For the projects in the multifamily rental program, the agency makes loans directly to developers.

Most Single-Family Home Loans Are Made to Households of Moderate Income

State law authorizes the agency to provide loans for the purchase of single-family homes for borrowers who meet income and other requirements. The income limits are based on median income data, which are then used to determine the limits for the very low, lower, and moderate income categories. However, state law also authorizes the agency to use higher limits when it finds that the higher limits are necessary to qualify a substantial number of households for its loans. Even though over the past several years the agency has established higher limits to qualify borrowers for loans from the proceeds of certain bond issues, these higher limits did not exceed federal limits. Between July 1, 1985, and June 30, 1990, under these guidelines the agency purchased approximately 21,600 single-family loans at an average sales price of approximately $84,300, more than 91 percent of which went to moderate income households and less than 9 percent to very low and low income households. Only 3 of the approximately 21,600 loans were not made to very low, lower, or moderate income households.

A Sufficient Number of Lower Income Units Have Been Set Aside, but the Agency Lacks Some Assurance That They Are Occupied by Qualified Tenants

Between July 1, 1985, and June 30, 1990, the agency made loans to developers of 47 multifamily rental projects that consisted of approximately 3,390 rental units. During this period, federal and state law established varying requirements for the percentage of units that had to be set aside for qualified tenants and varying requirements for the income limits that defined a qualified tenant. All 47 of the agency's regulatory agreements with the developers require units to be occupied or reserved for very low or lower income households. The number of units always met or exceeded the applicable state or federal law.

Even though the agency restricted more units for qualified tenants than the law required, some developers did not submit the reports required to verify the number of units in the development actually occupied by qualified tenants. Other projects submitted reports but did not include information on all units restricted for qualified tenants. According to the agency, the reporting by project managers was not completed primarily because local housing agencies verified the income of tenants at a number of projects. The projects are more accustomed to reporting this information to local housing agencies instead of to the agency. Further, some projects did not include information on vacant units that could have been counted as restricted for qualified tenants if the previous tenants had been qualified. Other projects reported that certain tenants met income requirements when, in fact, tenant income exceeded limits set by state law. The agency states that it is in the process of developing procedures to obtain the local agencies' information on the income of tenants more regularly and to assure all tenants meet income requirements.

The Agency Has Met Some of the Needs of the Statewide Plan but Not Others

During the last three fiscal years, the agency has generally complied with the requirements in the California Health and Safety Code to finance new housing and rental units for very low and lower income households in certain types of demographic areas of the State in the same general proportion as the breakdown of needs for new housing in these areas identified in the statewide plan. The agency has not, however, met the statewide plans'

identified need for rehabilitating existing housing. The number of very low and lower income units produced for elderly and certain other types of households were either more or less than the number recommended by the plan. No units for large households were financed even though this need is identified in the plan. In general, the agency has not been able to balance production of the different types of units recommended by the statewide plan because it has financed a relatively small number of multifamily rental projects.

Recommendations

To ensure that the appropriate number of units in multifamily rental projects are occupied by qualified tenants, the California Housing Finance Agency should take the following actions:

- For those projects for which local agencies verify tenant income, formalize in writing its agreements with the projects and the local agencies involved. The agency should include in these agreements a procedure whereby the local agencies will periodically certify the number of units occupied by qualified tenants; and

- Require projects with vacant units that had previously been occupied by qualified tenants to report this information on the vacant units to the agency.

Agency Comments

In its response, the Business, Transportation and Housing Agency stated that the California Housing Finance Agency (agency) operates as a lender, not as a developer or builder. The response further stated that the agency's activities are market driven and dependent on demand not only by the consumer in the housing market but also by builders in the development community and investors in the capital markets. The response also indicated that, in 1991, the agency expects to remedy the deficiencies noted in the report regarding units restricted to very low and lower income households. Furthermore, the response noted that the agency has instituted a regional allocation system to improve

single-family loan allocation in areas that have been proportionately low. Finally, the response confirmed that the agency has no single-family rehabilitation program, although it has studied the feasibility of such a program, and that the multifamily rehabilitation program has been affected by changes in federal law.

Introduction

The California Housing Finance Agency (agency) was created by the Zenovich-Moscone-Chacon Housing and Home Finance Act, as amended, to meet the housing needs of persons and families of low or moderate income within California. To accomplish this, the agency is authorized to issue bonds and other obligations and to use the proceeds from these issues for a variety of purposes. These purposes include making construction loans, property improvement loans, and mortgage loans to finance the development of housing. The agency is also authorized to purchase mortgage loans from qualified mortgage lenders. In general, the agency purchases loans to finance single-family homes, and it makes direct loans to developers to finance multifamily rental projects.

The bonds issued by the agency are not obligations of the State. The agency repays the bonds with the revenues it receives when borrowers make their loan payments. According to the agency's annual report, as of June 30, 1990, the agency has had the authority to have an aggregate principal of $4.65 billion in outstanding bonds or notes.

The agency is able to lend money at below-market interest rates in part because the interest it pays its bondholders is exempt from taxation under the provisions of the Internal Revenue Code. These bonds qualify for tax-exempt status if their proceeds are used in a manner consistent with certain requirements in the code. For example, at least 95 percent of the net proceeds must be used to finance mortgages for borrowers having had no ownership interest in their principal residence for the preceding three years, the borrowers' income must not exceed certain

limits, the price of the home must be within certain limits, and the borrowers must occupy the home as their principal residence. Similarly, a specific portion of a multifamily rental project financed with tax-exempt bonds must be set aside for rental to households whose income does not exceed certain limits.

The Internal Revenue Code limits the interest rate the agency can charge on its loans. The maximum effective rate of interest on the mortgages over the bond yield may not exceed 1.125 percent. The agency uses its revenues, which include loan fees and interest income from program loans and investments, to finance its operations and for special loan programs for very low and lower income households.

Section 50956 of the Health and Safety Code requires the agency to have a policy to conduct its operations be fiscally self-sufficient and to not require appropriations from the General Fund. Section 51000 states that the agency's expenditures from the California Housing Finance Fund shall not be subject to the supervision or approval of any other officer or division of state government. Section 51050 (f) exempts the agency from supervision by another division or officer of state government for the approval of its contracts related to bond issues, for the management, acquisition or disposition of any property, funds, assets or loans acquired with bond proceeds or held in trust for the benefit of the agency's bondholders, and for the financing of housing developments. This section also exempts the agency from following state requirements for the competitive bidding of contracts, although it does require the agency to take into consideration the applicable state policies regarding competitive bidding.

The agency has agreements with certain lending institutions to purchase the mortgages these institutions make to borrowers eligible for the agency's programs. According to agency documents, as of May 30, 1990, the agency had such agreements with 33 lending institutions throughout the State. Between July 1, 1985, and June 30, 1990, the agency purchased approximately 21,600 single-family home loans at an average

sales price of approximately $84,300. The original amount of which totals approximately $1.7 billion. Approximately 11,000 (51 percent) of these loans were for newly constructed homes and 10,600 (49 percent) were for the purchase of existing homes.

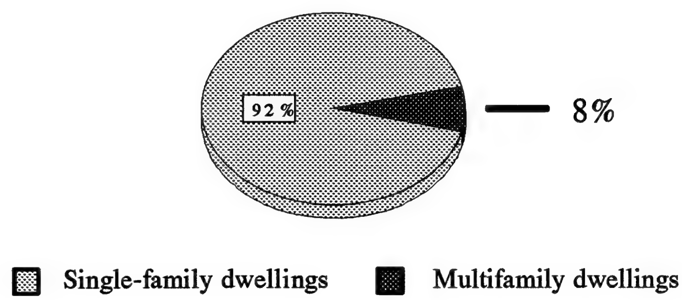
In addition to its Single-Family Home Loan Program, the agency has other programs that assist households with low incomes in purchasing homes. The Matching Down Payment Program and the Home Purchase Assistance Program allow the agency to provide a second loan to borrowers who have their first mortgage through the agency. The maximum loan under the Matching Down Payment Program is $5,000, and the maximum is $35,000 under the Home Purchase Assistance Program. The repayment of these loans, including interest, may be deferred for up to 30 years or until the home is sold or refinanced. Two other programs assist households with limited incomes. The Self-Help Housing Program allows the agency to offer mortgages at reduced interest rates to very low income households who work in groups under the supervision of a nonprofit self-help housing developer to construct their own homes. The Nonprofit Housing Program provides loans to nonprofit organizations that build single-family homes and then sell them to households with low incomes. In this review, we did not examine the loan applications for these programs for compliance with agency policies because these programs were outside the scope of our audit work.

For the single-family loan program, the agency purchases loans from other lenders, but for the construction of multifamily rental housing, the agency makes loans directly to developers. Generally, the agency makes mortgages with below-market interest rates available for those projects in which a percentage of the units are set aside for low income households. Between July 1, 1985, and June 30, 1990, the agency provided financing of $143.3 million to 47 multifamily rental projects. Figure 1 shows the agency's distribution of loans for single-family and multifamily unit.

Figure 1

The Distribution of Loans for Single-Family and Multifamily Units

Fiscal Years 1985-86 Through 1989-1990



Dollars Spent (in Millions)	
Single-Family dwellings	1,727
Multifamily dwellings	143
Total	1,870

In approving financing for the purchase of single-family home loans, the construction of multifamily rental projects, or the rehabilitation of housing units, Section 51225 of the Health and Safety Code directs the agency to balance its activities to meet statewide needs and, insofar as feasible, to provide financing in general proportion to the breakdown of certain housing needs identified in the California Statewide Housing Plan (statewide plan). Prepared by the California Department of Housing and Community Development (department), the statewide plan is a compilation of goals and objectives for the development of

housing in California. Implementing the goals of the statewide plan and providing housing in general proportion to the needs identified in the statewide plan are only 2 of 17 objectives Section 50952 of the Health and Safety Code mandates for the agency. The statewide plan documents the priorities the agency should utilize in approving financing for new construction, for multifamily units with rental assistance, and for the rehabilitation of existing housing units. The statewide plan provides the percentage of total units needed for three types of demographic areas of the State as well as for each metropolitan county. This percentage is known as "proportionate need."

Scope and Methodology

To determine whether the California Housing Finance Agency is fulfilling its responsibilities, we reviewed laws, regulations, and policies relating to financing the purchase of single-family home loans and to developing multifamily rental units. We reviewed reports the agency has issued and documents in the agency's files, and we interviewed the agency's officials and officials at the California Department of Housing and Community Development.

To determine whether the agency is limiting its purchases of single-family home loans to households with low or moderate income, we obtained copies of the agency's computer files for July 1, 1985, to June 30, 1990, and compared the incomes of the borrowers to income limits published in the California Code of Regulations and by the agency. We also performed data integrity tests to ensure that the data was accurate and that it correctly reflected the agency's loan activity.

To determine the number of multifamily rental units financed by the agency, we obtained copies of computer records of multifamily projects financed by the agency between July 1, 1985, and June 30, 1990.

To determine if the appropriate percentage of rental units were occupied by households whose incomes were within applicable limits, we first reviewed regulatory agreements and other documents that established the limits on tenant income.

Using copies of the agency's automated files, we then compiled statistics on the number of units restricted for low and moderate income households. Finally, we compared the incomes of the households to the income requirements in the California Code of Regulations and the agency's program bulletins.

To determine whether the agency was providing the financing for single-family and multifamily homes in the same general proportion as the breakdown of housing needs identified in the California Statewide Housing Plan, we compared the number, location, and type of homes financed by the agency between July 1, 1987, and June 30, 1990, to the requirements in the statewide plan.

We reviewed other areas of the agency's operations and found few weaknesses. These areas included the management of contracts and statements of economic interests filed by members of the agency's board of directors and by agency staff. We also reviewed the amounts of fund balance required to be reserved by statute and bond agreements. We did not find any instances of noncompliance in this area. Finally, we reviewed travel expense claims for all staff whose total travel expenses exceeded $5,000 between July 1, 1989, and June 30, 1990. We have issued a management letter to the agency on the agency's travel policies.

Chapter 1 Most Single-Family Home Loans Are Made to Households of Moderate Income

Chapter Summary

The California Housing Finance Agency (agency) provides loans at below-market interest rates to persons and families of low or moderate income for the purchase of single-family homes. Although the California Health and Safety Code establishes the income limits for the moderate income category, the agency has found it necessary to modify these limits as authorized by the code in order to qualify a substantial number of households for its loans. During the last five fiscal years, under these guidelines more than 91 percent of the agency's single-family home loans were made to moderate income households and less than 9 percent were made to very low and lower income households. We found that single-family home loans were made to ineligible households in only 3 of approximately 21,600 loans.

Background

Each year the United States Department of Housing and Urban Development (HUD) establishes the median income of given geographic areas of the State. The California Department of Housing and Community Development (department) uses these figures to determine the limits for the very low and lower income households as a percentage of the area median income. Generally, HUD defines very low income households as those earning no more than 50 percent of the area median income adjusted for family size. It defines lower income households as those earning no more than 80 percent of the area median income adjusted for family size.

Section 50093 of the California Health and Safety Code establishes the income limits for low or moderate income households. Persons and families of low or moderate income are those whose income does not exceed 120 percent of the area median income as determined by HUD and adjusted for family size. The code directs the department to transmit changes in the area median income and income limits to the Office of Administrative Law for publication in the California Code of Regulations.

The Agency Has Used Higher Income Limits

The agency may use higher income limits in a designated geographic area if it determines that 120 percent of the median income in that area is too low to qualify a substantial number of persons and families of low or moderate incomes for purchasing homes without subsidy. Section 50093 of the California Health and Safety Code allows the agency to use these higher income limits if it acts jointly with the department or has the concurrence of the secretary of the Business, Transportation and Housing Agency.

The agency established higher income limits in 1982. On October 14, 1982, the agency's board, which included the department's director, approved a bond issue that included an increase in the income limits. The new income limit for a household of four or more, for all areas of the State, was 150 percent of the county median income, compared to the old limit of 120 percent. The limit was increased from 108 to 135 percent of median for a household of three people, from 96 to 135 percent of median for a household of two people, and from 84 to 120 percent for a household of one person. According to the agency's director at the time, the income limits needed adjustment because the existing limits were unrealistic in the market and were not competitive with local government programs that had higher income limits.

On May 14, 1987, the agency again exercised the authority granted by Section 50093 of the California Health and Safety Code. At this time, the agency's board approved a resolution that

increased the income limit for moderate income households to 150 percent of county median income without regard to family size. The secretary of the Business, Transportation and Housing Agency concurred with this resolution. According to the resolution, the change was required because the agency determined that the then current income limits were too low to qualify a substantial number of persons and families for the purchase of a home in California without subsidy.

Impact of the 1986 Tax Reform Act on Agency Income Limits

The agency established new income limits to comply with the federal requirements for the mortgage revenue bonds it issued after August 15, 1986. The federal Tax Reform Act of 1986 established the income limit for borrowers of funds from tax-exempt bonds as the greater of 115 percent of the area median income or the statewide median income, not adjusted for family size. The act also established that for economically distressed areas of the State, called target areas, two thirds of the financing had to be provided to households with incomes that did not exceed 140 percent of applicable median income. The other one third could have been used without income limitations. Before this act there were no federal income limits.

Consequently, after the Tax Reform Act of 1986, the agency had two sets of income limits establishing the qualifications of borrowers for the mortgages the agency could purchase. The higher set of limits applied to all loans purchased with the proceeds of the bond series issued before August 15, 1986. The lower limits were used for all loans purchased with new bonds issued after August 15, 1986, beginning with 1988 Series A and B, dated January 1, 1988.

A subsequent amendment to the Tax Reform Act of 1986 required a further decrease in the income limits for eligible households. The Technical and Miscellaneous Revenue Act of 1988 reduced the income limit for a moderate income household of one or two persons to 100 percent of the applicable median family income. A higher limit of 120 percent was allowed for

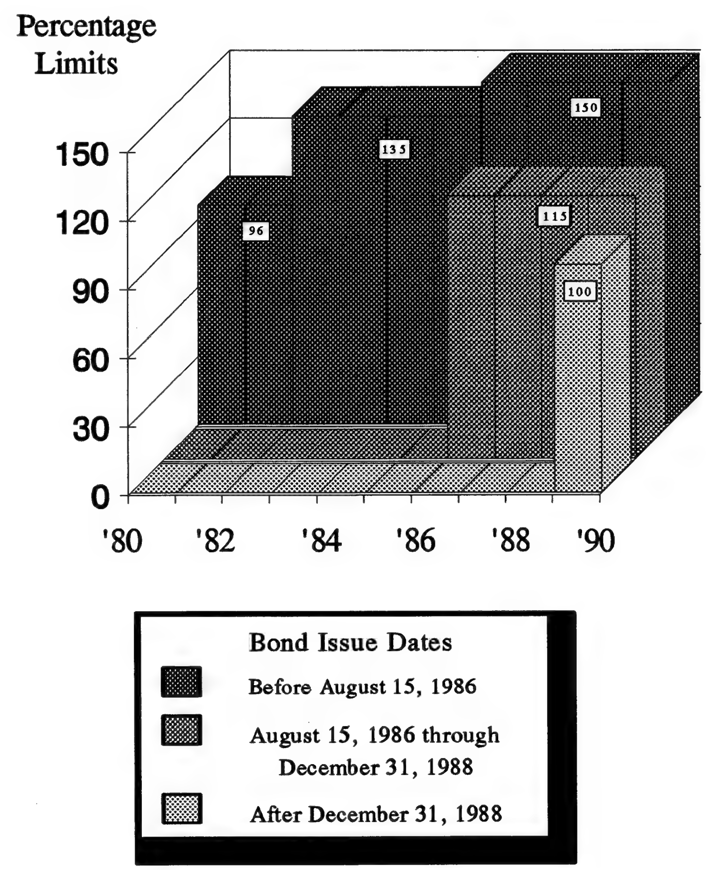
households of one or two persons in target areas. This act maintained the limit at 115 percent for households of three or more in nontarget areas and 140 percent for target areas. As a result of this change, the agency instituted a third set of income limits. All loans purchased with funds raised by bond issues beginning with 1989 Series A and B, dated April 1, 1989, were restricted to persons or households who met the new federal income limits.

Using a two-person household in a nontarget area as an example, Figure 2 compares the different income limits the agency used to qualify a household for an agency loan for the 10-year period ending June 30, 1990. Figure 2 also shows the income limits according to the California Code of Regulations for the same period. As Figure 2 shows, the income limits used to determine a household's eligibility for a loan depended on what bond series the lending institution used to fund the loan.

Figure 2

Income as a Percentage of Area Median Income on Bonds Issued for a Two-Person Household

1980 Through 1990

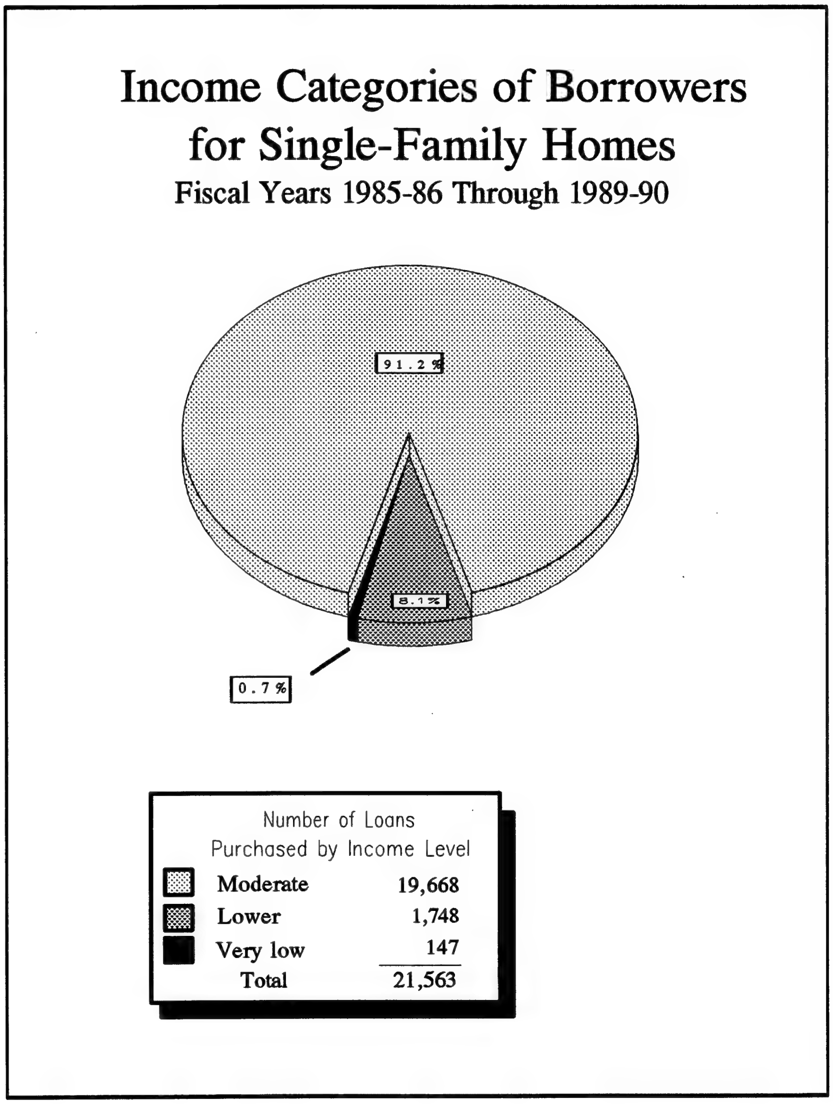


Note: Percentage limits are for nontarget areas.

The Agency Made Most of Its Loans to Moderate Income Households

As Figure 3 shows, in fiscal years 1985-86 through 1989-90, the agency purchased approximately 21,600 loans for single-family homes: 91.2 percent of its single-family home loans went to moderate income households, 8.1 percent to lower income households, and 0.7 percent to very low income households.

Figure 3



Furthermore, the number of loans the agency purchased for single-family homes increased from 2,057 in fiscal year 1985-86 to 5,406 in fiscal year 1989-90. As Table 1 shows, the number of loans to very low and lower income households also increased during this period. The average sales price, however, decreased.

Table 1 **The Number of Single-Family Home Loans Purchased by Fiscal Year and Income of Borrower**

Income of Borrower	1985-86	1986-87	1987-88	1988-89	1989-90	1985-86 Through 1989-90
Very low	1	9	35	46	56	147
Lower	53	43	356	686	610	1,748
Moderate	1,997	1,045	5,886	6,000	4,740	19,668
Other[a]	6	2		1		9
Total	**2,057**	**1,099**	**6,277**	**6,733**	**5,406**	**21,572**
Average sales price	$85,200	$87,800	$88,900	$80,700	$82,200	$84,300

[a]Includes three loans to borrowers with income in excess of the moderate level and six loans we identified as above the agency's limit for moderate income that could not be located for review.

In addition, we found that only rarely has the agency purchased loans made to ineligible households. Only 3 of approximately 21,600 loans were not made to very low, low, or moderate income households. According to the former director of programs, the agency's processing system is designed to prevent loans to people with above moderate incomes. These loans somehow slipped through the controls. However, federal law considers a bond to meet statutory requirements if the failure to meet federal requirements is corrected within a reasonable period after such failure is first discovered. As of July 1, 1991, the agency has not taken action to obtain financing that is not tax-exempt for the three loans made to ineligible borrowers.

Conclusion

From July 1, 1985, to June 30, 1990, the California Housing Finance Agency sometimes found it necessary to use higher income limits than the definitions established by the California Health and Safety Code to define low or moderate income households eligible for single-family home loans. During the same period, the agency had to adjust its limits to comply with changes in the federal requirements for tax-exempt mortgage revenue bonds. Under these guidelines, approximately 91.2 percent of the loans the agency purchased during this period were for the financing of homes for households with moderate incomes. Smaller percentages of the agency's loans, 8.1 percent and 0.7 percent, were purchased for financing lower income and very low income households respectively. The agency has generally ensured that loans have been made to households with incomes within the legal limits. However, the agency needs to correct the few instances of ineligibility we found.

Recommendation

The California Housing Finance Agency should take steps to have the three loans that we found were made to ineligible borrowers financed from bond revenues that are not tax-exempt.

Chapter 2 The California Housing Finance Agency Has Required Its Multifamily Rental Projects To Set Aside a Sufficient Number of Units for Lower Income Households but Lacks Some Assurance That the Appropriate Number of Units Are Occupied by Qualified Tenants

Chapter Summary

Between July 1, 1985, and June 30, 1990, the California Housing Finance Agency (agency) made loans to developers for 47 multifamily rental projects consisting of a total of approximately 3,390 rental units. During this period, federal and state laws established varying requirements regarding the income limits for qualified tenants and the percentage of units that must be set aside for them. All 47 of the agency's regulatory agreements with developers have met or exceeded applicable laws regarding the number of units that must be set aside for qualified tenants. However, seven projects did not submit reports to the agency containing the income levels of the tenants as required by the projects' regulatory agreements with the agency. Nineteen other projects have submitted reports that did not list a sufficient number of qualified tenants required to occupy units in the project according to the regulatory agreements.

Background

The California Health and Safety Code authorizes the agency to make loans for the construction or rehabilitation of multifamily rental housing projects. The code also requires that a percentage of the units in such projects be reserved for very low and lower income households. For those loans the agency finances with funds from the sale of tax-exempt bonds, the agency must also comply with federal requirements.

Both federal and state law have established income limits for those households that must occupy a percentage of units in a project. Similar to the income limits of the single-family housing program, the income limits of the multifamily rental projects

have varied depending on which statutory provision was in effect at the time the bonds were issued. Also varying was the percentage of units that had to be restricted to occupants whose income was within certain limits. For example, California law required that at least 20 percent of the units in a project located in a nontarget area had to be occupied by or reserved for lower income households. (Lower income households are currently defined as those having an income that did not exceed 80 percent of the area median income.) Further, beginning January 1, 1986, the California Health and Safety Code added the requirement that not less than half of the 20 percent required for lower income households should be occupied on a priority basis by very low income households. (Very low income households are currently defined as those having an income that did not exceed 50 percent of the area median.)

The federal Tax Reform Act of 1986 provided more stringent restrictions on tenant income. Beginning with all bonds issued after August 15, 1986, 40 percent or more of the units in a project had to be occupied by households with an income of 60 percent or less of the area median income. As an alternative, if developers did not want to reserve 40 percent or more of the units for these households with an income of 60 percent or less of the area median income, they could reserve 20 percent or more of the units for households with an income of 50 percent or less of the area median income.

The Agency's Agreements With Developers Met or Exceeded Applicable Statutes

Section 51335 of the California Health and Safety Code requires a developer who obtains financing through the agency from the proceeds of bonds to enter into a regulatory agreement with the agency. According to the statute, the agreement must provide that the units reserved for lower income households remain available to lower income households on a priority basis until the bonds are retired. Typically, these regulatory agreements specify the agency's requirements regarding the number or percentage of the project's rental units that must be occupied by or reserved for lower income households.

Between July 1, 1985, and June 30, 1990, the agency made loans to developers for the construction or rehabilitation of 47 multifamily rental projects consisting of approximately 3,390 rental units. All of the agency's regulatory agreements with the developers of these 47 projects required a number of units to be occupied by or reserved for lower income households that was equal to or greater than the number required by applicable state or federal statutes.[1] In fact, the number of units restricted by the agency's regulatory agreements for very low and lower income households (1,230) exceeded the number required by the applicable statutes (693) by 77 percent.

The Agency Must Ensure That All Units Are Occupied by Qualified Tenants

To ensure that units restricted for lower income households in multifamily rental units are actually occupied by households with appropriate income levels, the agency requires that borrowers obtain a certification of income from each prospective tenant of a dwelling unit designated for rental by a qualified tenant and send these certifications to the agency. In addition, on or before August 15 each year, borrowers are required to file a report with the agency specifying the total number of units in the development and the number of units occupied by qualified tenants as of the previous June 30. A qualified tenant is a household whose income is within the income limits specified in the regulatory agreement or an empty unit whose previous tenant was qualified.

On May 14, 1990, the agency sent a letter to each of the projects financed under its multifamily rental housing program, requesting that the borrower complete and return an income certification form for all qualified tenants. The form requires information on each tenant, including the tenant's family size and current annual income. According to the agency's director of

[1] One project's regulatory agreement did not meet the state requirement that 10 percent of the units be restricted to tenants with very low income. This project required that 100 percent of the units be occupied by tenants with 60 percent or less of the area median income. As of April 1, 1991, more than 10 percent of the units were occupied by very low income tenants.

administration, before that time, the agency had not routinely monitored the reporting requirements of the regulatory agreements.

Some Projects Did Not Submit Reports

As of April 1, 1991, the agency had not obtained reports from seven of its multifamily rental projects. These seven projects had regulatory agreements restricting a total of at least 89 units for lower income households. According to the agency's director of administration, the projects most likely did not send these reports to the agency because the projects were more accustomed to reporting this information to local housing agencies. At these projects, local agencies had assumed the responsibility of monitoring the income of tenants because the local agencies have assisted the projects in some way and, like the agency, have required that a portion of the projects' housing units be set aside for households of various income categories. In response to our inquiries, the agency's director of administration requested information from three local housing agencies that maintained records on qualified tenants in the seven projects. This information showed that the projects had more qualified tenants than required by the agency's regulatory agreements with the multifamily rental projects.

The director of administration stated that the agency is planning to formalize agreements with local agencies so that the local agencies will provide the agency with information on the income of qualified tenants each year. The agency's director of administration stated that the agency is also planning to modify the reporting requirements contained in the regulatory agreements with these seven projects to have them report the income of all qualified tenants directly to the local agencies instead of to the agency itself.

Some Reports Did Not List a Sufficient Number of Qualified Tenants

According to agency reports, another 19 projects submitted reports to the agency that did not list a sufficient number of qualified tenants to meet the number specified in the project's regulatory agreements. The agency's director of administration said that the reason 5 of these projects did not list more qualified tenants was that local agencies monitor these 5 projects. The agency has informal agreements with these projects to have them report to the agency only the number of qualified tenants necessary to ensure compliance with federal statutes. This number may be less than the number the regulatory agreement requires. The projects were to report the remaining number of qualified tenants only to the local agencies, not the agency itself. However, the agency plans to have local agencies monitor these projects and annually report the income of all qualified tenants to the agency.

The incomplete reports filed by 9 other projects did not include information on a total of 27 units that should have been occupied by qualified tenants. According to the agency's director of administration, these 27 units were most likely not reported because they were vacant at the time the report was requested. The agency had asked for information only on those units occupied by qualified tenants. However, the regulatory agreement defines a vacant unit as a qualified unit if the last occupant of the unit was a qualified tenant. Therefore, we believe that these 9 projects should have included information in their reports on vacant units that had previously been occupied by a qualified tenant. We attempted to verify that the 9 projects had at least 27 vacant units reserved for very low or lower income tenants. We were unable to verify that 27 units were qualified because the monthly vacancy report does not distinguish between units reserved for very low and lower income tenants and those units available without restrictions.

Seven of the nine projects that did not include information on all qualified tenants plus five other projects included in their reports 40 tenants who were not qualified to occupy units restricted to very low or lower income households. The household income for these tenants at the time they initially occupied the units exceeded the maximum income for lower income households as defined by the State. According to the agency's executive director, differences between federal and state requirements resulted in the agency not requiring income to be adjusted for family size for those projects that were financed by bonds issued before the Tax Reform Act of 1986.

Before August 15, 1986, the federal and state government had different income limits for low or moderate income households. The federal government did not require adjustments for family size and set its limit for low or moderate income households at 80 percent of the area median income. The State, however, did require adjustments for family size and based its income limits on data provided by the United States Department of Housing and Urban Development and published in the California Code of Regulations. For example, for a household of one, the state income limit was set at 56 percent of area median income for lower income households compared to the federal income limit of 80 percent.

The 40 tenants with incomes in excess of the limits for low income households met the federal requirements but did not meet the state requirements. According to the agency's executive director, the agency overlooked the more stringent state requirements in its efforts to ensure compliance with federal requirements. The agency's executive director stated that the agency has notified all affected projects of the problem. All projects will be required to verify that prospective tenants meet income limits that include adjustments for family size. Without complete information, the agency lacks some assurance that units set aside for lower income households are actually occupied by qualified tenants.

In contrast to the 26 projects that either failed to report or filed incomplete reports, the agency's reports on 20 of the remaining 21 multifamily rental projects indicated that the projects submitted the required annual reports on tenant income. The one project that did not submit an annual report was not completed.

Conclusion

The California Housing Finance Agency has executed regulatory agreements with developers that restrict the occupancy of multifamily rental projects as required by statute. From July 1, 1985, to June 30, 1990, the agency provided financing for 47 multifamily rental projects. The agency's regulatory agreements with developers set aside about 1,230 units (36 percent) of the approximately 3,390 units for occupancy by very low and lower income households. This amount exceeded the applicable statutory requirements. However, although the agency routinely monitored the reporting requirement of the regulatory agreements beginning May 14, 1990, as of April 1, 1991, it had not obtained the reports required by its regulatory agreements for 7 projects. The agency has also received reports for another 19 projects that did not list a sufficient number of qualified tenants. Some of these projects were also monitored by local agencies. According to the director of administration, the agency is developing procedures whereby local agencies that monitor tenant income can report their results to the agency. In addition, the agency is providing new income limits to project managers that reflect the adjustments for family size as required by state law.

Recommendations

To ensure that the appropriate number of units in its multifamily rental projects are reserved for or occupied by qualified tenants, the California Housing Finance Agency should take the following actions:

- For those projects where tenant income is verified by local agencies, formalize in writing its agreements with the projects and the local agencies involved. Include in these agreements a procedure whereby the local agencies will periodically certify the number of units occupied by qualified tenants;

- Require projects that have vacant units that had been previously occupied by qualified tenants to report this information to the agency, thereby ensuring that the projects comply with the regulatory agreements by having the required number of units occupied by or reserved for qualified tenants; and

- Require each project to verify that the initial income of all prospective tenants does not exceed the maximum income allowed for lower income families as adjusted for family size.

Chapter 3 The California Housing Finance Agency Has Met Some of the Needs of the California Statewide Housing Plan but Not Others

Chapter Summary

The California Statewide Housing Plan (statewide plan) identifies the number of housing units needed within three types of demographic areas of the State and for the State as a whole. The California Health and Safety Code requires that the California Housing Finance Agency (agency) balance its activities within these three types of demographic areas in the same general proportion as the breakdown of the State's needs for housing identified in the statewide plan. This proportion is known as "proportionate need." For the last three fiscal years, the agency has generally fulfilled the proportionate need set out in the statewide plan in financing new housing units and in financing the development of rental units for very low and lower income households. However, it has not always fulfilled the proportionate need in financing the development of new housing by county and in financing the rehabilitation of existing housing units.

Insofar as feasible, the California Health and Safety Code also requires the agency to finance, in the same general proportion to the breakdown of needs identified in the statewide plan, the development of housing designed for particular types of lower income households. The agency has financed a higher proportion of units for qualified elderly households than that required by the statewide plan. Furthermore, the agency has not financed the development of housing for large households, even though the statewide plan identifies a need for this type of housing. In addition, the agency's data does not allow us to determine whether it is meeting some of the detailed needs identified in the statewide plan for housing units for specific qualified households, such as those for persons with orthopedic disabilities, because it does not maintain data on its data base for some of the statewide

plan's specific needs. Finally, the agency has not financed the development of rental units by county for the elderly, regardless of income level, in the same general proportion as identified in the statewide plan. In general, we found that the agency has not been able to balance its activity in proportion to the breakdown of some of the needs in the statewide plan because it has been able to finance a relatively small number of multifamily rental projects.

The Agency Should Finance Housing in Proportion to Needs Identified in the Statewide Plan

Section 50450 et seq. of the California Health and Safety Code provides for the development of the California Statewide Housing Plan, which is updated biennially by the California Department of Housing and Community Development. The statutes require the plan to include a statement of housing goals, policies, and objectives, including targets, for the minimum number of units that should be built or rehabilitated in order to house all residents of the State in standard, uncrowded units in suitable locations. The statutes also require the plan to include goals for the minimum number of households that will need assistance to result in a substantial reduction in the number of lower income households paying more than 25 percent of their gross income for housing. The statewide plan's analysis of housing needs contains a chapter defining the priorities the agency should follow in financing housing units.

The statewide plan expresses one set of the agency's priorities as a proportion derived by dividing the number of housing units needed in a designated area in the State by the number of housing units needed in the State as a whole. This proportion is known as "proportionate need." For example, if the statewide plan indicated that County X needed 10,000 housing units and the State needed 100,000, then the proportionate need for County X was 10 percent (10,000/100,000). Therefore, County X should have received 10 percent of the units the agency financed in the State that year. If the agency financed 60,000 units throughout the State, then 6,000 of these should have gone to County X. Note that the agency is not required to finance all of the units needed in the county. Local agencies, other state agencies, and commercial lenders finance many of them.

To determine its primary priorities, the statewide plan divides the State into three types of demographic areas: urban metropolitan, rural metropolitan, and nonmetropolitan. A location is usually designated as either metropolitan or nonmetropolitan. Which portion of a metropolitan location is defined as urban or rural depends on the population of the area. According to the statewide plan, a rural area is one that, taken together with adjoining areas, has a population of less than 20,000. An urban area is defined in the California Health and Safety Code as an area which is not a rural area. All counties in California except San Francisco have rural areas. Section 51225 of the California Health and Safety Code requires the agency to balance its activities among these three types of demographic areas in the same general proportion as the breakdown of needs identified in the statewide plan.

The statewide plan expresses other agency priorities. The California Health and Safety Code requires the agency, insofar as feasible, to balance its financing in general proportion to other specific needs identified in the statewide plan. The needs specified in the plan include those determined by county and those determined by type of household. Implementing the goals of the statewide plan and providing housing in general proportion to the needs identified in the statewide plan are 2 of 17 objectives that Section 50952 of the Health and Safety Code mandates for the agency.

The Agency Met New Housing Needs by Demographic Area

Between July 1, 1987, and June 30, 1990, the agency generally financed the purchase or construction of new housing units in the same general proportion as the breakdown of needs established by the statewide plan for the three demographic areas into which it divides the State. We consider the agency to have generally met the needs established in the statewide plan if its activity was plus or minus 6 percent of the plan's proportionate need for that activity.

Dated August 1987, the statewide plan established the proportionate need for new housing units as follows: 78.0 percent for urban metropolitan areas, 13.0 percent for rural metropolitan areas, and 9.0 percent for nonmetropolitan areas. Between July 1, 1987, and June 30, 1990, the agency financed the purchase of 8,416 new homes and the construction of 1,564 new rental units for a total of 9,980 new housing units. These units were distributed as follows: 7,609 (76.2 percent) were urban metropolitan, 1,836 (18.4 percent) were rural metropolitan, and 535 (5.4 percent) were nonmetropolitan. Figure 4 and Figure 5 compare the proportionate need for new housing units in the three types of demographic areas with the proportion of new housing units the agency has actually financed in those areas.

Figure 4

The Percentage of New Housing Units by Type of Demographic Area

Fiscal Years 1987-88 Through 1989-90

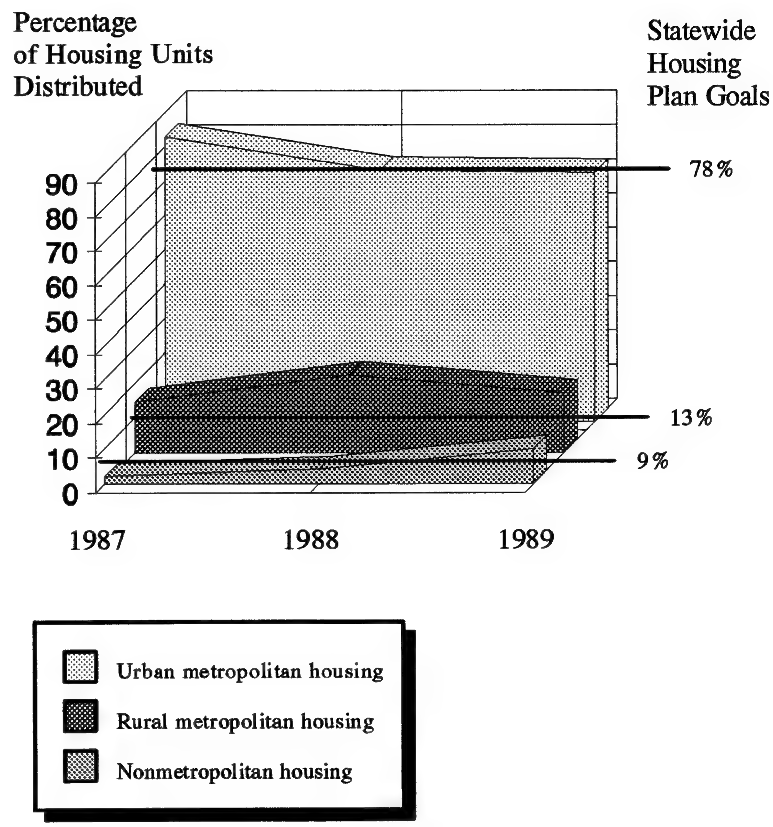
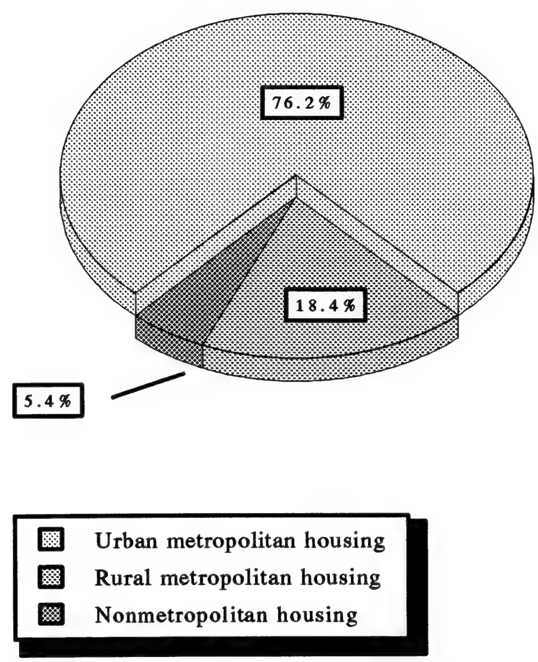


Figure 5

The Percentage of New Housing Units by Type of Demographic Area

Fiscal Years 1987-88 Through 1989-90



The Agency Did Not Meet New Housing Needs by County

Although the agency has generally met the proportionate need for new housing in the three demographic areas of the State as a whole, it has not met this need as closely in some individual counties. In addition to identifying the proportionate need for new housing units by demographic area, the statewide plan identifies the proportionate need for new housing units in each of the 31 metropolitan counties in the State. (The proportionate need for nonmetropolitan counties is not broken down by county

but given as a total for all nonmetropolitan counties.) The percentage of new housing units that the agency has financed in Los Angeles, San Diego, and Orange counties has been less than the proportionate need by more than 6 percent from July 1, 1987, to June 30, 1990. For example, the statewide plan designated that 17.54 percent of the housing units financed by the agency should have been built in Los Angeles County. However, only 7.74 percent of the new units constructed during this period were built in Los Angeles County, a difference of 9.8 percent. At the same time, the percentage of newly constructed housing financed by the agency in Sacramento, Fresno, Kern, and Tulare counties has generally been more than 6 percent more than the proportionate need for this same period. Figure 6 shows the counties that received more that 6 percent of their proportionate need of new housing units financed by the agency and those that received less that 6 percent in that period.

Counties With Greater Than 6 Percent Difference Between the Proportionate Need for New Housing and the New Housing Units Financed

Fiscal Years 1987-88 Through 1989-90

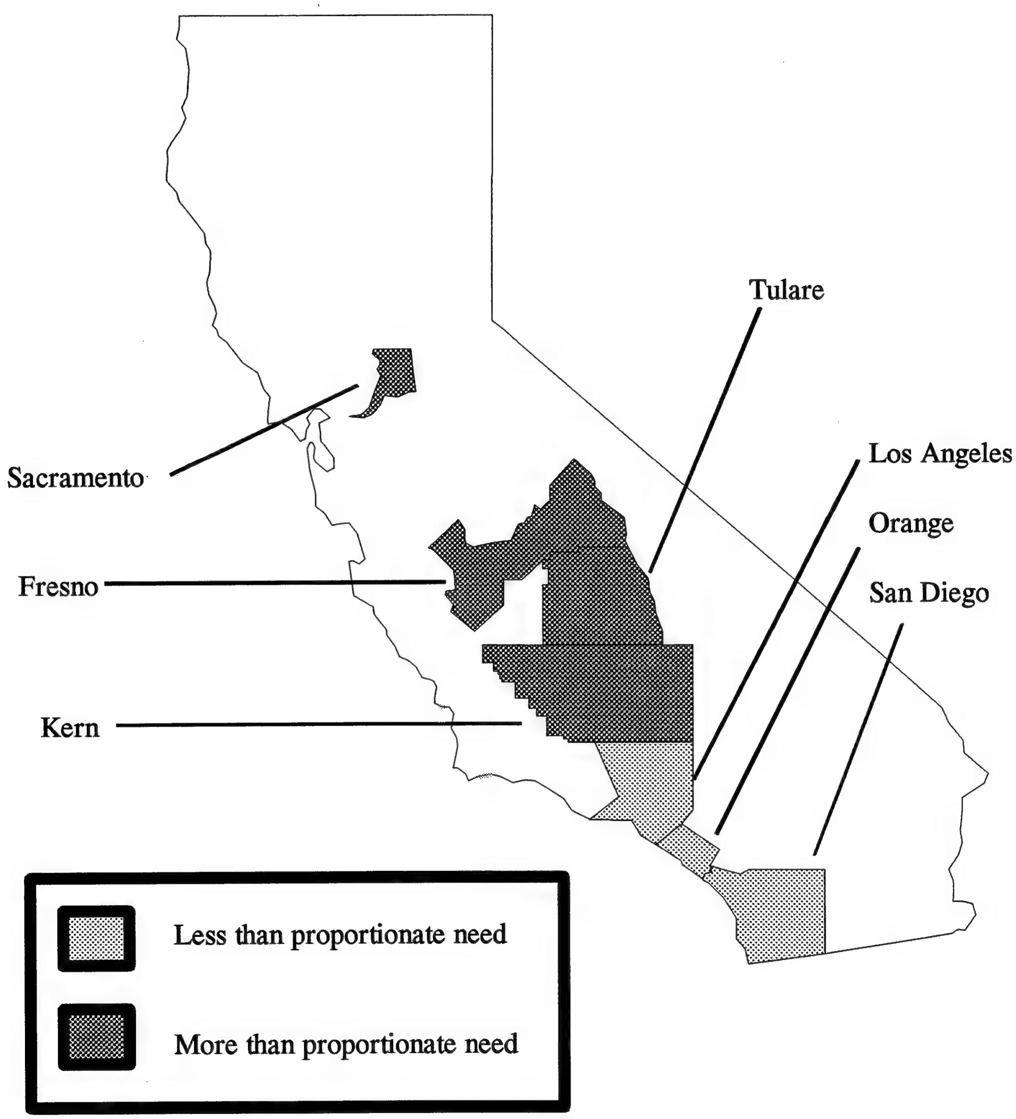


Figure 6

Appendix A compares the breakdown of needs established in the statewide plan with the agency's actual financing activity in each metropolitan county. According to the agency's executive director, the agency was not always able to meet the proportionate need for financing new housing in these counties primarily because there was less demand for its loans in the Los Angeles and San Diego counties and other counties with a high cost of housing. The price of houses in those areas often exceeded the agency's price limits or made it very difficult for first-time home buyers to qualify for loans to purchase the high-priced houses. There was more demand for the agency's single-family loans in those areas where houses were moderately priced. The executive director pointed out that the decline of demand for new housing financed by the agency's multifamily rental program further hindered the agency's efforts to meet all of the goals of the statewide plan.

The agency's executive director stated that he directed the agency to take steps to ensure that the number of single-family homes it finances in each county is proportionate to the breakdown of needs for new housing units by county as identified in the statewide plan. Beginning in 1989, the agency divided the State into six regions and, for each sale of bonds, established a set amount of loans to be financed in each region based on the region's population. This policy will reduce the number of houses financed in the central valley, where, in general, houses have been priced more moderately, and will provide more of the loan money for financing housing in proportion to the population.

The Agency Generally Met the Needs for Multifamily Rental Units for Very Low and Lower Income Households

The agency has financed the construction or rehabilitation of multifamily rental units for very low and lower income households that qualified for rental assistance in the same general proportion as the breakdown of needs for this type of housing identified in the statewide plan. Households that qualify for rental assistance are generally very low and lower income households that need

this assistance to maintain their rent at no more than 25 percent of their gross income. From July 1, 1987, to June 30, 1990, the agency provided financing for the construction or rehabilitation of approximately 1,590 multifamily rental units, 552 (35 percent) of which had to be rented to households who qualified for either rent subsidy from the federal government or reduced rental rates as set by the agency. Of these rental assistance units, 502 (91 percent) were located in urban metropolitan areas, and 50 (9 percent) were located in rural metropolitan areas. None of the units were located in nonmetropolitan areas. As Figure 7 and Figure 8 show, this activity generally meets the proportionate need identified in the statewide plan of 89 percent for urban metropolitan areas and 7 percent for rural metropolitan areas. However, the agency has not financed any units in nonmetropolitan areas, which had a proportionate need of 4 percent.

Figure 7

The Percentage of Rental Housing Units for Very Low and Lower Income Households by Type of Demographic Area

Fiscal Years 1987-88 Through 1989-90

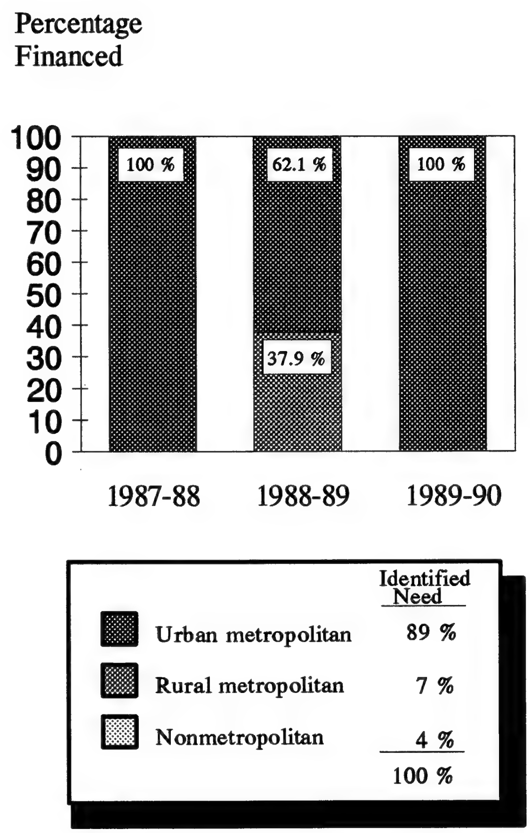
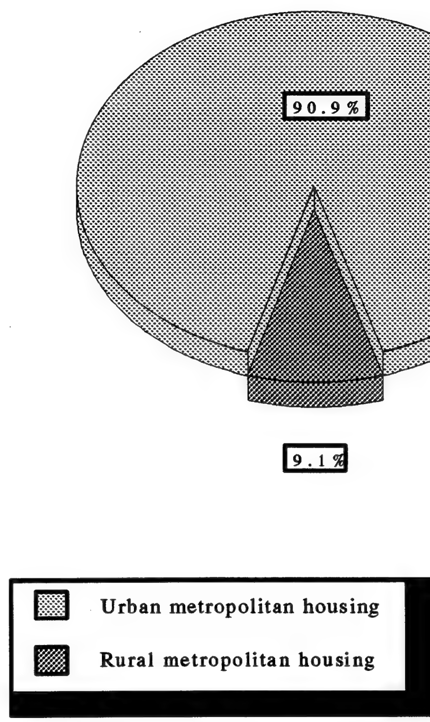


Figure 8

The Percentage of Rental Housing Units for Very Low and Lower Income Households Financed by the California Housing Finance Agency

Fiscal Years 1987-88 Through 1989-90



Further, the agency has not met the proportionate need for financing units for very low and lower income households in each county. The 552 units were located in 11 metropolitan counties. Because of the small number of units built in only 11 counties, a county by county comparison to the proportionate needs identified

in the statewide plan is not meaningful. The agency did not meet the needs of the statewide plan in the following metropolitan counties, even though they had relatively large proportionate needs identified by the statewide plan: Los Angeles County (36.4 percent), San Diego County (8.5 percent), and Orange County (7.7 percent).[2]

The Agency Did Not Meet All Needs for Housing Rehabilitation

The statewide plan also identifies the proportionate need for the rehabilitation of existing housing by type of demographic area. Between July 1, 1987, and June 30, 1990, the agency has financed the rehabilitation of only 187 housing units, all of which were part of four multifamily rental projects. Two of the projects were in Yolo County, one in Sacramento County, and the other in Santa Clara County.

The agency financed no rehabilitation projects in the following counties, even though they had relatively large proportionate needs identified by the statewide plan: Los Angeles County (30.0 percent), San Diego County (5.9 percent), Alameda County (4.8 percent), San Bernardino County (4.4 percent), and San Francisco County (4.0 percent).

According to the agency's executive director, the agency has no single-family rehabilitation program although it has studied the feasibility of such a program. In addition, the executive director stated that a multifamily rehabilitation program was developed with a major bank. The bank provided credit enhancement for the loans. This program became infeasible when the bank's credit rating was lowered.

---

[2] The agency has financed 94 units restricted for very low and lower income households in Los Angeles County. The unmet need was therefore 19.4 percent.

The Agency Met Some but Not All Needs of Special Households

In addition to identifying the proportionate need for rental units for households qualified for rental assistance by demographic area and by county, the statewide plan also identifies the need for these units by type of household. Section 51225 of the Health and Safety Code states that, insofar as feasible, the agency shall attempt to provide financing for housing specifically designed for particular types of lower income households in the same general proportion to the breakdown of needs identified in the statewide plan. These types of households include households with persons who are elderly or handicapped and large households with five or more persons needing 4 or more bedrooms. Table 2 shows the proportionate need of rental units restricted to qualified households identified in the statewide plan.

Table 2 Proportion of Housing Assistance Needed According to Household Type

Households	Percentage of Need	
Elderly Housing Units (Age 60 or more)		
Small households (0 to 3 bedrooms)	34.5%	
Large households (4 or more bedrooms)	0.6	
Subtotal Elderly		35.1%
Handicapped Housing Units (Not elderly)		
Orthopedic disability	5.0	
All other disabilities	3.9	
Subtotal Handicapped		8.9
All Other Housing Units		
Small household (0 to 3 bedrooms)	43.9	
Large household (4 or more bedrooms)	12.1	
Subtotal Other		56.0
Total		**100.0%**

Source: California Statewide Housing Plan, Phase I, August 1987

From July 1, 1987, to June 30, 1990, the agency financed a higher proportion of rental units for very low and lower income elderly than the need identified in the statewide plan, but it did not meet the proportionate need of the other identified groups as shown in Table 2. Of the 552 rental units restricted to qualified tenants the agency financed in that period, 291 (53.0 percent) were built for the elderly. The remaining 261 (47.0 percent) rental units were available for any other types of qualified households. We were not able to determine the number of handicapped units constructed for tenants qualified for rental assistance.

The agency maintains data on the number of rental units it has financed for the elderly and handicapped as well as a breakdown of the total number of units by household size (number of bedrooms). It does not, however, maintain data such that it can compare its activities with some of the specific needs identified in the statewide plan. Specifically, its data base does not identify the number of bedrooms in each of the rental units reserved for qualified tenants, nor does it maintain data that identify whether units for qualified tenants are designed for the handicapped.

It is clear, however, that the agency has not financed the development of rental units for large households who need rental assistance in the same general proportion to the breakdown of needs identified in the statewide plan. The statewide plan identifies the proportionate need for large household units for the elderly as 0.6 percent and the need for all other units designed for large households as 12.1 percent. However, between July 1, 1987, and June 30, 1990, the agency did not finance the development of any units designed for large households. According to the agency's former director of programs, the agency has tried to comply with the goals of the statewide plan regarding large households. He said that developers did not have an incentive to provide units with four or more bedrooms, however, because the larger units would have resulted in a smaller number of units in the project. Consequently, the developers would have received less income from the project than they would have received with a greater number of units designed for smaller households. Furthermore,

according to the agency's executive director, the 1986 and 1988 federal tax acts also compounded the difficulty of structuring three- and four-bedroom units into projects. The cost of larger units is inversely proportional to the income they generate, and with most tax incentives gone, developers became much more concerned about actual income and cash flow.

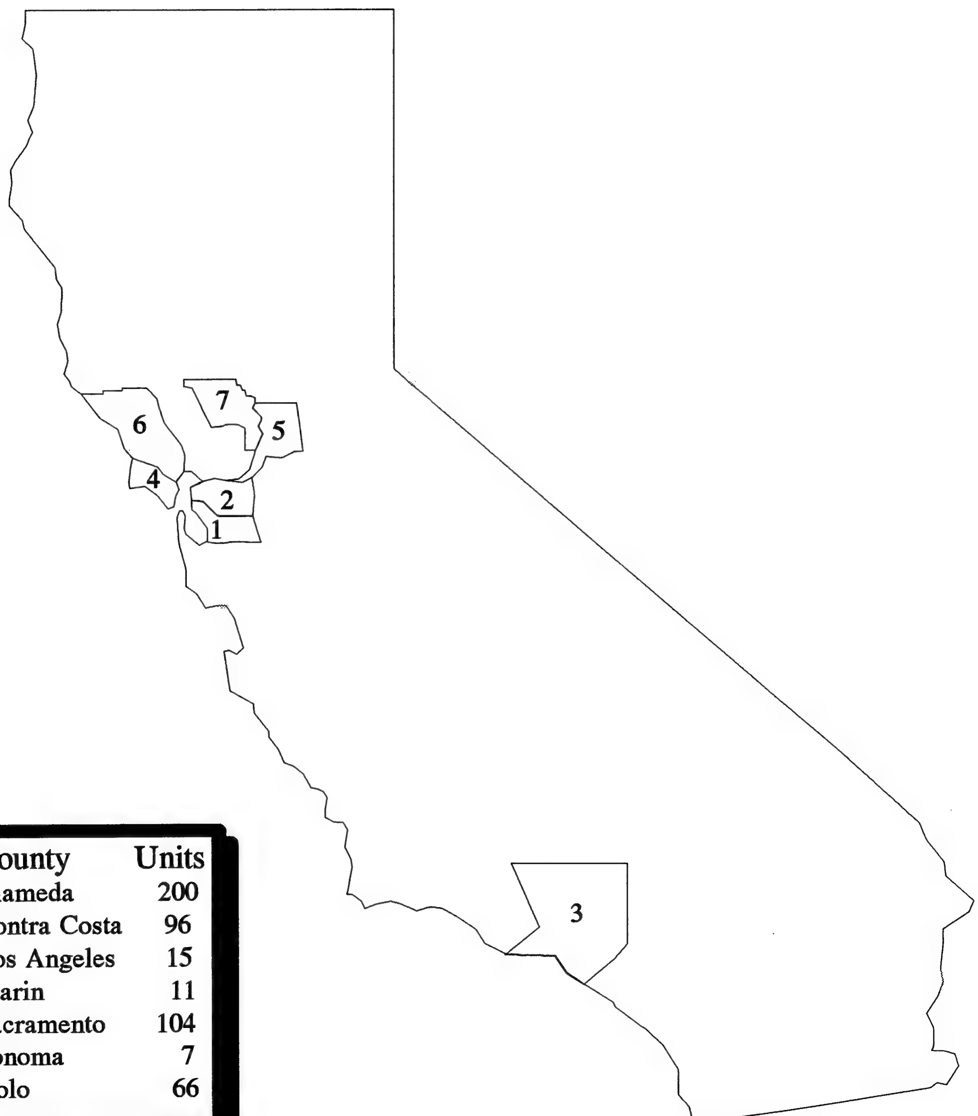
The Agency Did Not Meet the Rental Housing Needs for the Elderly by County

In addition to identifying the proportion of rental assistance units needed for rental by the elderly, the statewide plan also identifies by county the proportionate need for rental housing for all elderly in the State. During the last three fiscal years the agency has not met the proportionate need identified in the statewide plan for financing the construction or rehabilitation of rental units for the elderly by county.

Of the 24 multifamily rental projects the agency financed in fiscal years 1987-88 through 1989-90, seven projects were built for the elderly. These seven projects were located in seven different counties and had a total of 499 rental units. The seven counties and the number of elderly units the agency financed in those counties is shown in Figure 9.

The Number of Rental Housing Units for the Elderly Financed by the California Housing Finance Agency

Fiscal Years 1987-88 Through 1989-90



	County	Units
1.	Alameda	200
2.	Contra Costa	96
3.	Los Angeles	15
4.	Marin	11
5.	Sacramento	104
6.	Sonoma	7
7.	Yolo	66

Figure 9

The agency had not financed the development of housing units for the elderly in the following counties, even though these counties had a proportionate need of more than 3 percent: San Diego County (7.6 percent), Orange County (6.4 percent), San Francisco County (4.1 percent), Santa Clara County (3.9 percent), Riverside County (3.8 percent), and San Bernardino County (3.6 percent). See Appendix B for the statewide plan's proportionate need for elderly housing.

The proportionate need for nonmetropolitan counties is not broken down by county but given as a total for all nonmetropolitan counties. The statewide plan identifies the proportionate need for all nonmetropolitan counties as 5.8 percent. The agency did not finance the development of any elderly units in nonmetropolitan counties.

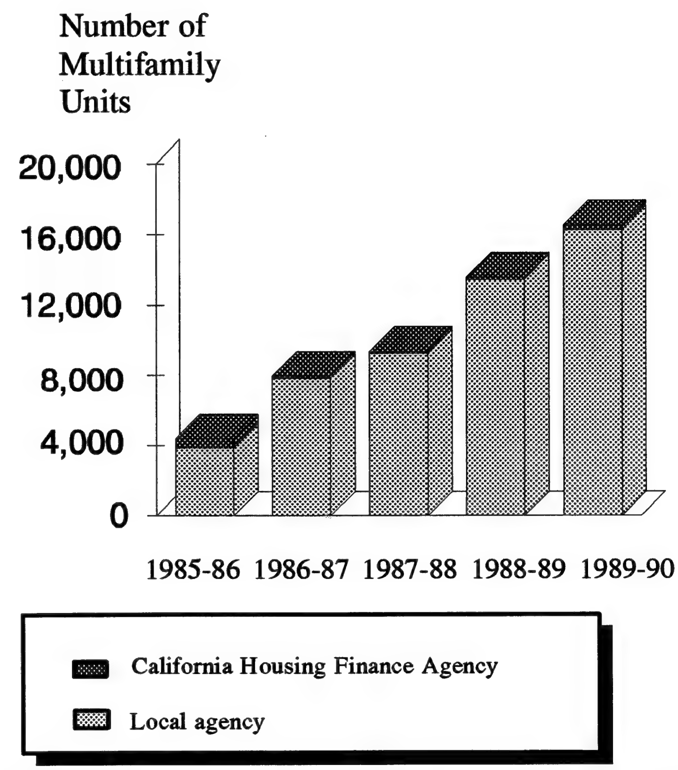
Lack of Multifamily Rental Projects Contributed to the Agency's Inability To Meet Some Needs of the Statewide Plan

According to the agency's executive director, the primary reason that the agency has not met some of the needs in the statewide plan for multifamily rental units for households that qualify for housing and multifamily housing units for the elderly in general is that, since the Tax Reform Act of 1986, the agency has financed relatively few multifamily rental projects. According to the agency's executive director, the agency's ability to meet the goals and objectives of the statewide plan is a function of market forces and of changes in federal law relative to tax-exempt bond financing. The executive director also stated that the developers were more inclined to obtain financing for their multifamily housing projects from local housing agencies or commercial lenders than from the agency. As Figure 10 shows, data reported by the California Debt Advisory Commission indicates that between July 1, 1987, and June 30, 1990, local agencies provided financing for more than 10,000 multifamily rental units reserved for lower income households. According to the agency's executive director, developers willing to build low-income units preferred to work with local agencies because the agency requires a longer regulatory period to ensure maintenance of lower income units and because the local agencies provided financial enhancements, such as reduced developer fees or grants of land, that the agency could not.

Figure 10

Sources of Financing for Multifamily Units Restricted to Very Low and Lower Income Households

Fiscal Years 1985-86 Through 1989-90



Note: The number of units financed by local agencies was calculated from cumulative data published in California Debt Advisory Commission Annual Summary Reports: The Use of Housing Bond Revenue Proceeds.

Recently, the agency has had an increase in its lending activity for multifamily units. According to unaudited agency data from July 1989 through March 1991, the agency has approved financing for three projects containing an estimated 122 units reserved for lower income households. The agency also has committed funds for an additional 32 projects that developers have submitted for

approval. These projects consist of 739 units reserved for lower income households. The agency's executive director attributes this increase to the inability of developers to obtain financing for multifamily projects from commercial lenders and to the curtailment in multifamily lending by banks and thrifts.

Conclusion

The California Housing Finance Agency has generally been successful in balancing its financing of newly constructed housing among urban metropolitan, rural metropolitan, and nonmetropolitan areas in the same general proportion as the breakdown of needs identified in the California Statewide Housing Plan.

Although the agency's financing of new housing units in some individual counties has deviated more than 6 percent from the proportionate need identified in the plan, the agency has implemented a new regional allocation process that should help correct this situation. The agency has done little in financing the rehabilitation of existing single-family housing units because it believes that a program to rehabilitate single-family homes requires more monitoring than it has the capability to provide. Further, primarily because the agency has financed relatively few multifamily rental projects, the agency has not met the proportionate need identified in the statewide plan in two other areas: housing for large households who qualify for housing assistance and housing for elderly in certain counties. The agency attributes the lack of activity in its multifamily program to the developers' preference for local agencies to finance their multifamily projects and to a general downturn in multifamily development. Finally, the agency does not maintain its data base in sufficient detail to allow it, or anyone else, to determine the extent to which it finances activities consistent with some of the more specific needs identified in the statewide plan, such as providing housing for persons with orthopedic disabilities.

Recommendation

To allow the evaluation of multifamily housing provided for specific types of households as required by the California Statewide Housing Plan, the California Housing Finance Agency should revise its data base to include sufficient detail to enable it to compare its financing activities with all categories of need identified in the statewide plan.

We conducted this review under the authority vested in the auditor general by Section 10500 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully submitted,

KURT R. SJOBERG
Auditor General (acting)

Date: July 29, 1991

Staff: Steven L. Schutte, Audit Manager
Thomas A. Sachs
Jiyoung Kim

Appendix A

The Difference Between the Proportion of New Housing Units Financed by the California Housing Finance Agency and the Proportionate Need Identified by the California Statewide Housing Plan July 1, 1987 to June 30, 1990

Metropolitan Counties	Proportionate Need	Proportion Financed	Difference
Alameda	2.68%	2.17%	- 0.51%
Butte	0.92	0.62	- 0.30
Contra Costa	2.52	3.18	0.66
El Dorado	1.23	0.29	- 0.94
Fresno	1.69	18.43	16.74
Kern	1.79	7.01	5.22
Los Angeles	17.54	7.73	- 9.81
Marin	0.88	0.23	- 0.65
Monterey	1.31	0.25	- 1.06
Napa	0.39	0.05	- 0.34
Orange	10.75	0.75	-10.00
Placer	1.41	2.80	1.39
Riverside	5.18	5.77	0.59
Sacramento	3.80	16.09	12.29
San Bernardino	6.45	3.75	- 2.70
San Diego	11.94	2.86	- 9.08
San Francisco	0.32	0.36	0.04
San Joaquin	0.89	1.25	0.36
San Mateo	1.34	0.97	- 0.37
Santa Barbara	0.92	0.88	- 0.04
Santa Clara	4.68	1.91	- 2.77
Santa Cruz	1.20	0.00	- 1.20
Shasta	0.65	0.13	- 0.52
Solano	1.94	0.94	- 1.00
Sonoma	1.83	1.90	0.07
Stanislaus	1.23	4.44	3.21
Sutter	0.25	0.00	- 0.25
Tulare	1.11	6.77	5.66
Ventura	3.82	0.18	- 3.64
Yolo	0.60	2.93	2.33
Yuba	0.18	0.01	- 0.17
Total Metropolitan Counties	91.44	94.65	
Nonmetropolitan Counties	8.56%	5.35%	
Total	**100.00%**	**100.00%**	

Appendix B

The Difference Between the Proportion of Elderly Housing Units Financed by the California Housing Finance Agency and the Proportionate Need Identified by the California Statewide Housing Plan July 1, 1987 to June 30, 1990

Metropolitan Counties	Proportionate Need	Proportion Financed	Difference
Alameda	4.60%	40.10%	35.50%
Butte	0.90	0.00	- 0.90
Contra Costa	2.10	19.20	17.10
El Dorado	0.40	0.00	- 0.40
Fresno	2.10	0.00	- 2.10
Kern	1.70	0.00	- 1.70
Los Angeles	30.50	3.00	-27.50
Marin	0.90	2.20	1.30
Monterey	1.10	0.00	- 1.10
Napa	0.50	0.00	- 0.50
Orange	6.40	0.00	- 6.40
Placer	0.50	0.00	- 0.50
Riverside	3.80	0.00	- 3.80
Sacramento	3.10	20.90	17.80
San Bernardino	3.60	0.00	- 3.60
San Diego	7.60	0.00	- 7.60
San Francisco	4.10	0.00	- 4.10
San Joaquin	1.60	0.00	- 1.60
San Mateo	2.50	0.00	- 2.50
Santa Barbara	1.30	0.00	- 1.30
Santa Clara	3.90	0.00	- 3.90
Santa Cruz	1.00	0.00	- 1.00
Shasta	0.60	0.00	- 0.60
Solano	0.70	0.00	- 0.70
Sonoma	1.50	1.40	- 0.10
Stanislaus	1.10	0.00	- 1.10
Sutter	0.20	0.00	- 0.20
Tulare	1.10	0.00	- 1.10
Ventura	1.70	0.00	- 1.70
Yolo	0.40	13.20	12.80
Yuba	0.20	0.00	- 0.20
Total Metropolitan Counties	94.20[a]	100.00	
Nonmetropolitan Counties	5.80%	0.00%	
Total	**100.00%**	**100.00%**	

[a]The total of the proportionate need for metropolitan counties is taken from the California Statewide Housing Plan. The sum of the counties is 91.7 percent. However, we cannot account for the error in addition.

1120 N Street
Sacramento
95814

(916) 445-1331

Alcoholic Beverage Control
Banking
Corporations
California Highway Patrol
California Housing Finance Agency
Commerce

PETE WILSON
GOVERNOR
STATE OF CALIFORNIA

Housing and Community Development
Motor Vehicles
Real Estate
Savings and Loan
Transportation
Teale Data Center
Office of Traffic Safety
Office of Small Business Advocate

BUSINESS, TRANSPORTATION AND HOUSING AGENCY

July 25, 1991

Mr. Kurt R. Sjoberg
Auditor General (Acting)
660 J Street, Suite 300
Sacramento, CA 95814

Dear Mr. Sjoberg:

Subject: P-950 - "The California Housing Finance Agency Has Generally Complied With Statutory Requirements in Financing Single-Family Homes and Multifamily Rental Projects"

I have reviewed the findings and recommendations contained in a draft report by the Office of the Auditor General (P-950) entitled "The California Housing Finance Agency Has Generally Complied With Statutory Requirements in Financing Single-Family Homes and Multifamily Rental Projects." We offer the following comments on the draft report;

The California Housing Finance Agency (the "Agency") operates as a lender, not as a developer or builder. As such, its activities are market-driven and dependent on demand not only by consumers in the housing market, but also by builders in the development community and investors in the capital markets. The Agency does not have subsidy funds and is not a grant-making organization, nor is it unilaterally able to create housing in the market sectors where need may exist; it has only limited resources at its disposal, namely below-market interest rate loans, to entice developers to build such housing.

The Agency's ability to meet the goals and objectives of the Statewide Housing Plan is a function of market forces and of changes in federal law relative to tax exempt bond financing. These are the factors which make a given project "feasible" or not. The Plan relates only to a very small part of the goals and objectives the Agency is mandated to "seek to attain" and only

"insofar as feasible." For example, the 1986 tax Reform Act removed most of the investment incentives and caused a sudden and serious drop-off in all types of residential rental housing production. After 1986, the Agency had enough difficulty financing lower income units at all, and even more difficult for the various sub-interest groups such as "orthopedic disability handicapped" housing or "large elderly households."

The period of 1985-90 was also a period of excessive home price escalation, adding yet another factor to the uncertainty of developer/investor confidence and the severity of new federal tax legislation. The interaction of all these factors contributed to the Agency's difficultly financing multifamily housing and single-family housing in high-cost areas. In the multifamily area, the 1986 and 1988 federal tax acts also compounded the difficulty of structuring three and four bedroom units into projects. The cost of larger units is inversely proportional to the income they generate, and with most tax incentives gone, developers became much more concerned about actual income and cash flow. Developers became much less willing to build low-income housing in general, and large-bedroom configurations in particular. During the period of 1985-90 there was a general, industry-wide downturn in the production of multifamily units altogether.

Recommendations of the report relative to property management were undertaken by the Agency on its own initiative concurrently with moving the Property Management Division from San Francisco to Sacramento in late 1989. In 1990, comprehensive procedures for monitoring occupancy were developed and instituted, including a yearly reporting cycle. Deficiencies cited in the report are accurate and expected to be remedied in the 1991 cycle, data for which was unavailable to the Auditor-General at the time of preparation of this report.

The Agency has simultaneously endeavored to eliminate duplicative reporting by projects to both local and state entities in instances where local occupancy requirements are more restrictive than state requirements. Agreements formalizing this process and modifying existing agreements are proposed to be in place prior to the next yearly reporting cycle.

The Agency has also modified its vacancy reports for the 1991 reporting cycle, and the projects have received income limits specific to each individual project for determining qualifying income of tenants. This adjustment will correct the problem of underreporting or misreporting occupancy by qualifying tenants.

The number of single-family units produced in the audit period for Los Angeles, Orange and San Diego Counties may have been proportionately low. Prior to completion of the audit, however, the Agency instituted a regional allocation system on its own initiative which will drastically improve single-family loan originations in areas which has been proportionately low.

The Agency has no single-family rehab program although it has studied the feasibility of such a program. A multifamily rehab program was developed with a major bank in which the bank would have provided the credit enhancement for the loans. This program became infeasible when the bank's credit rating was lowered. Federal law relative to multifamily rehab changed in the mid-eighties to limit the use of tax-exempt bonds to instances of acquisition accompanied by "substantial rehabilitation," defined to be at least 15% of the total project cost. Rehab without acquisitions, i.e. upon refinancing, is no longer allowed.

If you have any questions regarding these comments or would like any additional information please call me at 445-2794.

Sincerely,

A. A. PIERCE
Undersecretary

cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps